

## Tax Policy

Tax policy has an impact on the lives of all Americans. Whether one is buying a home, having a child, trading stocks, or saving for a rainy day, tax implications will affect an individual's future finances and therefore must be weighed. While taxes are necessary to generate revenue to ensure the strength and security of our country, our tax code should be simple and fair.

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- Internal Revenue Service
- Joint Committee on Taxation

### Tax Cuts

Since being elected, President Bush has made reducing taxes a major theme of his Administration. While most Americans would agree that they pay too much in taxes, the tax cuts pursued by this Administration have favored the wealthiest in America while leaving those in low- and middle-income brackets with limited relief. In addition, the Bush tax cuts have led to a reduction in revenue of over \$870 billion from 2001 to September 2005, turning record surpluses into record deficits and leaving the responsibility of paying for these deficits to future generations. The Administration wants to permanently extend the tax cuts and has imposed steep cuts in services (Medicaid, student loans, food stamps, etc.) to people who depend on them to partially cover the cost of the tax cuts. Lastly, these tax cuts have had the unintended effect of forcing more middle-income taxpayers to pay the Alternative Minimum Tax (AMT), an alternative tax method originally designed to ensure that the very wealthy did not escape their full tax liability by using tax shelters and by claiming excessive deduction. The result for some middle-income taxpayers is that many important tax deductions are lost to the AMT.

Rep. Eshoo has supported tax cuts that are fiscally responsible by being fully offset and that target tax relief at the people who need it most.

## Alternative Minimum Tax (AMT)

The AMT is a complicated and frequently inequitable tax which has created significant tax burdens for many taxpayers across the country. The AMT was originally designed to prevent high-income taxpayers from escaping their "fair" share of the income tax burden through excessive deductions and tax shelters. Under the AMT, deductions from taxable income are not permitted, including deductions for State and local taxes. Therefore, Californians are hit especially hard when they are forced to pay the AMT.

The alternative minimum tax for individuals is calculated in the following manner. First, an individual adds back various tax preference items to his or her taxable income under his regular income tax. This gross amount then becomes his tax base for the AMT. Next, the amount of the basic exemption is calculated and subtracted from the AMT tax base. A two-tiered tax rate structure of 26 and 28% is then assessed against the remaining AMT tax base to determine AMT tax liability. The taxpayer then pays whichever is greater, his regular income tax liability or his AMT tax liability.

Because the AMT was never indexed for inflation, every year more and more taxpayers are threatened by AMT liability, whether they know it or not. Congress has continued to intervene on a temporary basis to spare middle-income taxpayers, while ignoring the long-term implications of this tax. The Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) increased the basic AMT exemption amount to \$58,000 for joint returns and to \$40,250 for unmarried taxpayers in order to provide relief for taxpayers who were never intended to be affected by this tax. Unfortunately, this temporary extension expired on December 31, 2005. To extend this provision, Rep. Eshoo led her Colleagues in a letter to House and Senate Conferees on H.R. 4297, the Tax Relief Extension Reconciliation Act of 2005, urging them to include an extension of the AMT exemption. If an extension is not included, 19 million American taxpayers will be subject to the AMT.

### AMT and Stock Options

The AMT has also had a disastrous impact on individuals who have participated in employee incentive stock options (ISOs), which are common in Silicon Valley. Employees who receive ISO's pay the AMT on the difference between market value of the stock at the time of exercise and the price they paid through their ISO. For example, if an employee exercises an option to buy stock at \$1 per share and the current market value were \$10 per share they would be liable for AMT payments on \$9 per share. Unfortunately, because the tech bubble burst after many people had exercised their stock options but before they actually sold their stock, some taxpayers are literally facing hundreds of thousands of dollars in tax liability based on income they have never seen. Despite this fact, there is nothing in current law that allows these stockholders to recoup the taxes they paid on profits they never realized.

In response to this situation, Rep. Eshoo is a cosponsor of H.R. 3385, the AMT Credit Fairness Act. The bill would begin providing refunds to taxpayers with AMT credits more than four years old. Qualifying taxpayers would receive rebates at either 20 percent or \$5,000 per year, whichever is greater.

Because of the importance of this issue, Rep. Eshoo joined her Colleagues in sending a letter to Conferees on H.R. 4297, the Tax Relief Act, urging for the inclusion of H.R. 3385 in the final Conference Report on this legislation. While H.R. 3385 was not included in the Conference Report, Rep. Eshoo has pledged to continue to work to provide relief to these taxpayers.

## Additional resources:

- Rep. Eshoo's letter to Conferees regarding inclusion of the AMT into the Conference Report to H.R. 4297
- Rep. Eshoo's letter to Conferees regarding the inclusion of H.R. 3385 into the Conference Report of H.R. 4297
- IRS's "AMT Assistant"

## Estate Tax

The estate tax is assessed on estates valued at over \$2 million for individuals upon the death of the owner. While Rep. Eshoo does not believe in unlimited sums being transferred from one generation to the next without any tax, she has supported efforts to provide relief from the estate tax to ensure that families and small business owners can transfer their business assets and homes to their heirs. This is a particularly important issue for California's 14th Congressional District where property values are high.

Under provisions of the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001, the estate tax is gradually phased out and ultimately zeroed-out by January 1, 2010. However, because EGTRRA expires December 31, 2010, the estate tax would then revert back to its original levels. Rep. Eshoo voted against this bill because she believed a total repeal was excessive and that reinstating the full tax in 2010 was unfair.

To provide fairness and certainty to taxpayers Rep. Eshoo cosponsored H.R. 1577, the Certain and Immediate Estate Tax Relief Act. This legislation increases the current exclusion amounts to \$3 million for individuals in 2006 and makes the 2009 level permanent at \$3.5 million, thereby exempting 99.7 % of all estates in America from estate tax liability.

Instead, the House passed H.R. 8, the Estate Tax Permanency Repeal Act, in 2005. This legislation completely repeals the estate tax for all estates, including billionaires, at a cost of \$292 billion over the next ten years. Rep. Eshoo opposed passage of this legislation in part because of its impact on our already skyrocketing deficit. The Senate is expected to offer its own proposal on the estate tax in 2006.

## Research and Development Tax Credit

The Research and Development (R&D) tax credit provides companies with incentives to invest in research and development activities. This credit has proven to be enormously successful in assisting companies devote capital to generating the new products and ideas that energize our entire economy. Unfortunately, Congress has continued to provide this credit through periodic extensions. In order to ensure that companies can continue to benefit from this credit, Rep. Eshoo has cosponsored H.R. 1736, the Investment in America Act. This bill permanently extends the R&D tax credit while establishing a new category within the R&D tax credit that enables companies to take full advantage of the benefits. This was one of the key elements of the House Democrats Innovation Agenda, which Rep. Eshoo helped craft.

Rep. Eshoo has also called for renewing the current R&D tax credit which expired on December 31, 2005. Unless the credit is extended, companies will lose a very important incentive to investing in the future technologies of this country.

#### Additional resources:

- Rep. Eshoo's letter to House leaders on the R&D tax credit
- House Democrats' Innovation Agenda

#### Tax Reform

Among the President's announced goals upon taking office was reforming our current tax code. To that end, the President established a panel to analyze our current system. The panel was ordered to issue a revenue neutral report that simplifies the current code, reduces the cost of compliance, shares the tax burden in an appropriately progressive manner, promotes long-run economic growth and job creation, and better encourages work, saving, and investment.

In November of 2005, the Panel issued its report and two proposals for reform; the Simplified Income Tax Plan and the Growth and Income Tax Plan. Both plans share several common points (such as the elimination of the Alternative Minimum Tax); however, they differ in the taxation of businesses and personal income. More information on the panel, its report and subsequent proposals can be found at [www.taxreformpanel.gov/index.shtml](http://www.taxreformpanel.gov/index.shtml).

Rep. Eshoo remains very concerned about some of the Panel's recommendations, particularly limitations on mortgage deductions, however, these proposals are simply that: proposals. In order to change any aspect of our tax code, legislation would have to be introduced and passed into law. To date, no legislation has been introduced to act upon the Panel's recommendations.